

**Montabella Community Schools
Edmore, Michigan**

FINANCIAL STATEMENTS

June 30, 2007

Montabella Community Schools

Edmore, Michigan

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June 30, 2007

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Montabella Community Schools

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INDEPENDENT AUDITOR'S REPORT

To the Board of Education
Montabella Community Schools
Edmore, Michigan

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of and for the year ended June 30, 2007, which collectively comprise the District's financial statements as listed in the table of contents. These financial statements are the responsibility of Montabella Community Schools' management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of June 30, 2007, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 13, 2007 on our consideration of Montabella Community Schools' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis and budgetary comparison information, as identified in the table of contents, are not a required part of the financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Montabella Community Schools' financial statements. The accompanying other supplementary information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the financial statements. The other supplementary information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Abraham & Gaffney, P.C.

ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

September 13, 2007

Montabella Community Schools

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2007

This section of the Montabella Community School's annual financial report presents our discussion and analysis of the School District's financial performance during the year ended June 30, 2007. Please read it in conjunction with the School District's financial statements, which immediately follow this section.

Using this Annual Report

This annual report consists of a series of financial statements and notes to those statements. These statements are organized so the reader can understand Montabella Community Schools financially as a whole. The **district-wide** financial statements provide information about the activities of the whole School District, presenting both an aggregate view of the School District's finances and a longer-term view of those finances. The **fund** financial statements provide the next level of detail. For governmental activities, these statements tell how services were financed in the short-term as well as what remains for future spending. The fund financial statements look at the School District's operations in more detail than the district-wide financial statements by providing information about the School District's most significant funds, the General Fund and the Site and Facilities Sinking Fund, with all other funds presented in one column as nonmajor funds. The remaining statements (the Statement of Fiduciary Net Assets and the Statement of Changes in Fiduciary Net Assets) present financial information about activities for which the School District acts solely as an agent for the benefit of students and parents. The structure of the financial statements is as follows:

Management's Discussion and Analysis (MD&A)
(Required Supplementary Information)

Basic Financial Statements

District-wide Financial Statements Fund Financial Statements

Notes to the Financial Statements

(Required Supplementary Information)
Budgetary Information for Major Funds

Other Supplementary Information

Reporting the School District as a Whole - District-wide Financial Statements

One of the most important questions asked about the School District is, "As a whole, what is the School District's financial condition as a result of the year's activities?" The statement of net assets and the statement of activities, which appear first in the School District's financial statements, report information on the School District as a whole and its activities in a way that helps you answer this question. We prepare these statements to include all assets and liabilities, using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the School District's net assets - the difference between assets and liabilities, as reported in the statement of net assets - as one way to measure the School District's financial health or financial position. Over time, increases or decreases in the School District's net assets - as reported in the statement of activities - are indicators of whether its financial health is improving or deteriorating. The relationship between revenues and expenses is the School District's operating results. However, the School District's goal is to provide services to our students, not to generate profits as commercial entities do. One must consider many other non-financial factors, such as the quality of the education provided, the condition of the district's assets and the safety of the schools, to assess the overall health of the School District.

The statement of net assets and the statement of activities report the governmental activities for the School District, which encompass all of the School District's services, including instruction, support services, community services, athletics and food services. Property taxes, unrestricted State aid (foundation allowance revenue), and State and federal grants finance most of these activities.

Montabella Community Schools

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2007

Reporting the School District's Most Significant Funds - Fund Financial Statements

The School District's fund financial statements provide detailed information about the most significant funds - not the School District as a whole. Some funds are required to be established by State law and by bond covenants. However, the School District establishes many other funds to help it control and manage money for particular purposes (the Food Service and Athletics Funds are examples) or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money (such as bond-funded construction funds used for voter-approved capital projects). The governmental funds of the School District use the following accounting approach:

Governmental funds - All of the School District's services are reported in governmental funds. Governmental fund reporting focuses on showing how money flows into and out of funds and the balances left at year-end that are available for spending. They are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the operations of the School District and the services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the School District's programs. We describe the relationship (or differences) between governmental activities (reported in the statement of net assets and the statement of activities) and governmental funds in reconciliations.

The School District as Trustee - Reporting the School District's Fiduciary Responsibilities

The School District is the trustee, or fiduciary, for its student activity funds and private purpose trust funds. All of the School District's fiduciary activities are reported in separate statements of fiduciary net assets and changes in fiduciary net assets. We exclude these activities from the School District's other financial statements because the School District cannot use these assets to finance its operations. The School District is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

The School District as a Whole

Recall that the statement of net assets provides the perspective of the School District as a whole. Table 1 provides a summary of the School District's net assets as of June 30, 2007 with comparative information as of June 30, 2006:

Table 1

	Statement of Net Assets June 30, 2007	Statement of Net Assets June 30, 2006
Assets		
Current and other assets	\$ 3,951,231	\$ 3,794,307
Capital assets, net of accumulated depreciation	<u>12,337,331</u>	<u>12,717,605</u>
Total Assets	16,288,562	16,511,912
Liabilities		
Current Liabilities	2,726,187	2,872,934
Noncurrent Liabilities	<u>8,956,153</u>	<u>9,501,260</u>
Total Liabilities	11,682,340	12,374,194
Net Assets		
Invested in capital assets, net of related debt	2,876,751	2,703,024
Restricted	841,740	689,054
Unrestricted	<u>887,731</u>	<u>745,640</u>
	<u>\$ 4,606,222</u>	<u>\$ 4,137,718</u>

Montabella Community Schools

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2007

The analysis in Table 1 focuses on the net assets of the district. The affect on net assets as a result of the fiscal year activities is reflected in Table 2.

The School District's net assets were \$4,137,718 at June 30, 2006 and \$4,606,222 at June 30, 2007 (Table 1). Net assets have increased by \$468,504.

Capital assets, net of related debt totaling \$2,876,751 compares the original cost, less depreciation of the School District's capital assets, to long-term debt used to finance the acquisition of those assets. Capital assets also reflect investments in capital assets from operating funds. Most of the debt will be repaid from voter-approved property taxes collected as the debt service comes due. Durant loan obligations of the State are included in Long-Term obligations of the School District. Restricted net assets are reported separately to show legal constraints from debt covenants and enabling legislation that limit the School District's ability to use those net assets for day-to-day operations. Restricted Net Assets reflect the Debt Service fund balances less accrued interest on long-term debt as of June 30, 2007 in the amount of \$241,214 and the fund balance of the Site and Facilities Sinking Fund in the amount of \$600,526. Unrestricted Net Assets reflect those assets available to the school district for use in its operation.

The \$887,731 in unrestricted net assets of governmental activities represents the *accumulated* results of all past years' operations. The unrestricted net assets balance enables the School District to meet working capital and cash flow requirements as well as to provide for future uncertainties. The operating results of the General Fund will have a significant impact on the change in unrestricted net assets from year to year.

The results of this year's operations for the School District as a whole are reported in the condensed statement of activities (Table 2), which shows the changes in net assets for fiscal year 2006/07.

Table 2	Fiscal Year Ended June 30, 2007	Fiscal Year Ended June 30, 2006
Revenue		
Program Revenue:		
Charges for services	\$ 211,254	\$ 230,616
Operating Grants	1,495,290	1,668,848
Capital Grants	14,280	47,207
General Revenue:		
Property Taxes	2,372,613	2,425,311
School state aid - unrestricted	6,018,626	5,727,559
Other	<u>256,378</u>	<u>211,523</u>
Total Revenue	10,368,441	10,311,064
Functions/Program Expenses		
Instruction	4,867,699	4,948,611
Support Services	3,250,047	3,271,599
Food Service	413,832	445,582
Athletics	189,346	208,661
Transfers to other districts	143,801	131,416
Interest and costs on long-term debt	484,316	212,455
Unallocated depreciation	<u>550,896</u>	<u>572,661</u>
Total Expenses	<u>9,899,937</u>	<u>9,790,985</u>
Increase in Net Assets	<u>\$ 468,504</u>	<u>\$ 520,079</u>

Montabella Community Schools
MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2007

As reported in the Statement of Activities, the cost of all of our *governmental* activities this year was \$9,899,937. Certain activities were partially funded from those who benefited from the programs (\$211,254 charges for services) or by other governments and organizations that subsidized certain programs with operating and capital grants and contributions (\$1,509,570). We paid for the remaining "public benefit" portion of our governmental activities with \$2,372,613 in taxes (for General & Debt Service funds) and \$6,275,004 in State foundation allowance and other revenues, i.e., interest and general entitlements.

As discussed above, the net cost shows the financial burden that was placed on the State and the School District's taxpayers by each of these functions. Since property taxes for operations and unrestricted State aid constitute the vast majority of district operating revenue sources, the Board of Education and administration must annually evaluate the needs of the School District and balance those needs with State-prescribed available unrestricted resources.

The School District's Funds

As we noted earlier, the School District uses funds to help it control and manage money for particular purposes. Looking at funds helps the reader consider whether the School District is being accountable for the resources taxpayers and others provide to it and may provide more insight into the School District's overall financial health.

As the School District completed this year, the governmental funds reported a combined fund balance of \$1,795,558, which is an increase of \$332,249 from last year.

In the General Fund, our principal operating fund, the fund balance increased \$159,979 to \$809,192. General Fund fund balance is available to fund costs related to allowable school operating purposes. Montabella Community Schools uses its Fund Balance to "smooth" unexpected changes in revenues and/or expenditures.

Our Special Revenue Funds fund balances increased \$23,747 to \$61,375. Special Revenue Funds include the Food Service and Athletics Funds.

The Debt Service Funds showed a fund balance increase of approximately \$6,949, and the Capital Projects Funds fund balances increased by \$141,574.

General Fund Budgetary Highlights

Over the course of the year, the School District revises its budget as it attempts to deal with unexpected changes in revenues and expenditures. State law requires that the budget be amended to ensure that expenditures do not exceed appropriations. The final amendment to the budget was actually adopted just before year-end. A schedule showing the School District's original and final budget amounts compared with amounts actually paid and received is provided in required supplementary information of these financial statements.

General Fund Expenditures:

The District's budget for expenditures changed as follows during the year:

		<u>Percent</u>
Total Expenditures Original Budget	\$ 8,606,283	100.0
Total Expenditures Final Budget	<u>8,630,056</u>	<u>100.3</u>
Increase in Budget Expenditures	<u>\$ 23,773</u>	<u>0.3</u>

The District's actual expenditures were less than the final budget by \$243,522 or 2.8 percent.

Montabella Community Schools
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2007

Revenue Change from Original to Final Budget:

		<u>Percent</u>
Total Revenues Original Budget	\$ 8,421,495	100.0
Total Revenues Final Budget	<u>8,553,000</u>	<u>101.6</u>
Increase in Budget Revenues	<u>\$ 131,505</u>	<u>1.6</u>

The District's final actual general fund revenues differed from the final budget by \$6,487, a variance of (.08%) from the final budget.

Capital Assets and Debt Administration

Capital Assets

As of June 30, 2007, the School District had \$19,243,019 invested in a broad range of capital assets, including buildings and improvements, vehicles, and equipment. This amount represents a net increase (including additions and disposals) of \$163,525 from last year.

	<u>2007</u>	<u>2006</u>
Vehicles	75,690	67,788
Buildings and improvements	16,827,167	16,716,589
Equipment	<u>2,340,162</u>	<u>2,295,117</u>
Total historical cost	<u>\$ 19,243,019</u>	<u>\$ 19,079,494</u>

This year's additions of \$191,913 included office equipment and various building improvements. No new debt was issued for these additions.

Debt

At the end of this year, the School District had \$9,835,700 in bonds and other obligations outstanding versus \$10,380,598 in the previous year. Those obligations consisted of the following:

	<u>2007</u>	<u>2006</u>
General Obligation Bonds	\$ 9,685,000	\$ 10,260,000
Durant Resolution Bonds	69,435	69,435
Notes and Loans	-	1,605
Severance pay	<u>81,265</u>	<u>49,558</u>
Total	<u>\$ 9,835,700</u>	<u>\$ 10,380,598</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2007

Economic Factors and Next Year's Budgets and Rates

Our elected Board of Education and our administration considered many factors when setting the school district's 2006/07 fiscal year budgets. The one most important, but unpredictable factor, is our student count. The State Foundation Revenue is determined by multiplying the blended count by the foundation allowance per pupil. The blended count for the 2007 year is established by a legislatively set percentage of the fall and winter counts. About 67% of the total general fund revenue is from the State Foundation Allowance. The school district can no longer assess additional property tax revenue for general operations. This funding configuration makes the district funding heavily dependent on the State's ability to fund local school operations. Early enrollment projections at the beginning of the 2007/08 academic year indicate continuation of an ongoing decline in enrolment and likelihood of fifteen to twenty-five fewer students than in the 2006/07 school year as well as fifty to sixty fewer students than were estimated in 2006/07 budgetary planning. Once the final count and related per pupil funding rate is established, State law requires the school district to amend the budget if actual district resources are not sufficient to fund original appropriations.

The school district's revenue is greatly dependent on State funding and the status of the State's School Aid Fund. The actual revenue received depends on the State's ability to collect revenues as projected to fund its appropriation to school districts. As noted in previous years, because of revenue shortfalls, the State was unable to fund schools in accordance with the School Aid Act and therefore necessarily discounted foundation allowance allocations. We are cautiously aware of the reality it may happen again this school year. Other factors affecting the 2007/08 school year are increases in health insurance and in the District's contribution to the State Retirement System. Changes in staffing, elevated costs to provide special education services, and increased costs for employee contracts likewise had impact on initial budget projections.

Contacting the District's Management

This financial report is intended to provide our taxpayers, parents, and investors with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have any questions about this report or need additional information, we welcome you to contact the Montabella Community Schools central office which is located at 302 West Main Street, Edmore, Michigan.

BASIC FINANCIAL STATEMENTS

Montabella Community Schools

STATEMENT OF NET ASSETS

June 30, 2007

	Governmental Activities
ASSETS	
Current assets	
Cash and cash equivalents	\$ 2,506,005
Accounts receivable	14,254
Due from other governmental units	1,316,157
Inventories	9,751
Prepays	6,707
	<hr/>
Total current assets	3,852,874
Noncurrent assets	
Deferred charges, net of amortization	98,357
Capital assets, net of accumulated depreciation	12,337,331
	<hr/>
Total noncurrent assets	12,435,688
	<hr/>
TOTAL ASSETS	16,288,562
LIABILITIES	
Current liabilities	
Accounts payable	27,622
Accrued payroll	374,731
Other accrued liabilities	239,958
Due to other governmental units	315,005
Short-term note payable	1,100,000
Current portion of accrued interest	71,159
Current portion of accrued severance payable	20,316
Current portion of long-term debt	577,396
	<hr/>
Total current liabilities	2,726,187
Noncurrent liabilities	
Noncurrent portion of accrued interest	12,020
Noncurrent portion accrued severance payable	60,949
Noncurrent portion of long-term debt	8,883,184
	<hr/>
Total noncurrent liabilities	8,956,153
	<hr/>
TOTAL LIABILITIES	11,682,340
NET ASSETS	
Invested in capital assets, net of related debt	2,876,751
Restricted for debt service	241,214
Restricted for sinking fund activity	600,526
Unrestricted	887,731
	<hr/>
TOTAL NET ASSETS	\$ 4,606,222
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See accompanying notes to financial statements.

Montabella Community Schools

STATEMENT OF ACTIVITIES

Year Ended June 30, 2007

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenues and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental activities					
Instruction	\$ 4,867,699	\$ 12,385	\$ 1,054,703	\$ 11,760	\$ (3,788,851)
Supporting services	3,250,047	31,858	133,644	-	(3,084,545)
Food service	413,832	133,052	306,943	-	26,163
Athletics	189,346	33,959	-	2,520	(152,867)
Transfers to other districts	143,801	-	-	-	(143,801)
Interest and costs on long-term debt	484,316	-	-	-	(484,316)
Unallocated depreciation	550,896	-	-	-	(550,896)
TOTAL EXPENSES	\$ 9,899,937	\$ 211,254	\$ 1,495,290	\$ 14,280	(8,179,113)
General Revenues					
Property taxes					2,372,613
State school aid - unrestricted					6,018,626
Investment earnings					106,902
Special Education county allocation					18,589
Miscellaneous					130,887
TOTAL GENERAL REVENUES					8,647,617
CHANGE IN NET ASSETS					468,504
Net assets, beginning of year					4,137,718
Net assets, end of year					\$ 4,606,222

See accompanying notes to financial statements.

Montabella Community Schools

GOVERNMENTAL FUNDS BALANCE SHEET

June 30, 2007

	General	Site and Facilities Sinking	Nonmajor Governmental Funds	Total Governmental Funds
ASSETS				
Cash and cash equivalents	\$ 1,393,092	\$ 600,526	\$ 512,387	\$ 2,506,005
Accounts receivable	14,059	-	195	14,254
Due from other funds	105,979	-	-	105,979
Due from other governmental units	1,316,157	-	-	1,316,157
Inventories	-	-	9,751	9,751
Prepays	6,707	-	-	6,707
TOTAL ASSETS	\$ 2,835,994	\$ 600,526	\$ 522,333	\$ 3,958,853
LIABILITIES AND FUND BALANCES				
LIABILITIES				
Accounts payable	\$ -	\$ -	\$ 27,622	\$ 27,622
Accrued payroll	374,731	-	-	374,731
Other accrued liabilities	239,958	-	-	239,958
Due to other funds	-	-	105,979	105,979
Short-term note payable	1,100,000	-	-	1,100,000
Due to other governmental units	312,113	-	2,892	315,005
TOTAL LIABILITIES	2,026,802	-0-	136,493	2,163,295
FUND BALANCES				
Reserved for				
Inventories and prepaids	6,707	-	9,751	16,458
Debt service	-	-	324,393	324,393
Unreserved				
Undesignated, reported in				
General fund	802,485	-	-	802,485
Special revenue funds	-	-	51,624	51,624
Capital projects funds	-	600,526	72	600,598
TOTAL FUND BALANCES	809,192	600,526	385,840	1,795,558
TOTAL LIABILITIES AND FUND BALANCES	\$ 2,835,994	\$ 600,526	\$ 522,333	\$ 3,958,853

See accompanying notes to financial statements.

Montabella Community Schools

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO
THE STATEMENT OF NET ASSETS

June 30, 2007

Total fund balance - governmental funds **\$ 1,795,558**

Amounts reported for the governmental activities in the statement of net assets are different because:

Noncurrent assets used in governmental activities are not financial resources
and therefore are not reported as assets in the governmental funds.

The cost of capital assets is	\$ 19,243,019	
Accumulated depreciation is	<u>(6,905,688)</u>	12,337,331
Deferred charges, net of amortization		98,357

Long-term liabilities are not due and payable in the current period
and therefore are not reported as liabilities in the funds.

Long-term liabilities at year-end consist of:

Deferred amounts on refunding	293,855	
Bonds payable	(9,754,435)	
Accrued interest payable	(83,179)	
Severance pay	<u>(81,265)</u>	<u>(9,625,024)</u>

Net assets of governmental activities **\$ 4,606,222**

See accompanying notes to financial statements.

Montabella Community Schools

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES -
GOVERNMENTAL FUNDS

Year Ended June 30, 2007

	General	Site and Facilities Sinking	Nonmajor Governmental Funds	Totals Governmental Funds
REVENUES				
Local sources	\$ 1,305,804	\$ 293,364	\$ 1,226,706	\$ 2,825,874
State sources	6,660,592	-	37,207	6,697,799
Federal sources	526,808	-	264,651	791,459
TOTAL REVENUES	8,493,204	293,364	1,528,564	10,315,132
EXPENDITURES				
Current				
Instruction	4,835,992	-	-	4,835,992
Supporting services	3,268,868	-	-	3,268,868
Food service	-	-	413,832	413,832
Athletics	-	-	189,346	189,346
Debt service				
Principal retirement	1,874	-	575,000	576,874
Interest, fiscal and other charges	-	-	455,678	455,678
Capital outlay	-	151,801	-	151,801
TOTAL EXPENDITURES	8,106,734	151,801	1,633,856	9,892,391
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	386,470	141,563	(105,292)	422,741
OTHER FINANCING SOURCES (USES)				
Transfers from other funds	-	2,374	135,999	138,373
Other transactions	53,309	-	-	53,309
Transfers to other funds	(135,999)	-	(2,374)	(138,373)
Payments to other districts	(143,801)	-	-	(143,801)
TOTAL OTHER FINANCING SOURCES (USES)	(226,491)	2,374	133,625	(90,492)
NET CHANGE IN FUND BALANCES	159,979	143,937	28,333	332,249
Fund balances, beginning of year	649,213	456,589	357,507	1,463,309
Fund balances, end of year	<u>\$ 809,192</u>	<u>\$ 600,526</u>	<u>\$ 385,840</u>	<u>\$ 1,795,558</u>

See accompanying notes to financial statements.

Montabella Community Schools

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

Year Ended June 30, 2007

Net change in fund balances - total governmental funds \$ 332,249

Amounts reported for governmental activities in the statement of activities are different because:

Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:

Capital outlay	\$ 191,913
Net effect of disposal of capital assets	(21,291)
Depreciation expense	<u>(550,896)</u>

Excess of depreciation expense and other charges over capital outlay (380,274)

Repayment of long-term debt and borrowing of long-term debt is reported as expenditures and other financing sources in governmental funds, but the repayment reduces long-term liabilities and the borrowings increase long-term liabilities in the statement of net assets. In the current year, these amounts consist of:

Deferred charges - net current year amortization	(30,169)
Bond and loan principal retirement	<u>576,605</u>

Excess of bond principal retirement over bond proceeds 546,436

Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:

Decrease in accrued interest payable	1,800
(Increase) in accrued severance pay	<u>(31,707)</u>
	<u>(29,907)</u>

Change in net assets of governmental activities \$ 468,504

See accompanying notes to financial statements.

Montabella Community Schools

Fiduciary Funds

STATEMENT OF FIDUCIARY NET ASSETS

June 30, 2007

	Private Purpose Trust Fund	Agency Fund
ASSETS		
Cash	\$ 1,447	\$ 113,499
Investments	40,346	19,381
TOTAL ASSETS	41,793	\$ 132,880
LIABILITIES		
Due to individuals		
High School	-	\$ 74,764
Middle School	-	15,312
Webb Elementary	-	1,898
Blanchard Elementary	-	1,931
Preschool	-	35,446
Blanchard 5th Grade	-	3,529
TOTAL LIABILITIES	-0-	\$ 132,880
NET ASSETS		
Held in trust for private purposes	\$ 41,793	

See accompanying notes to financial statements.

Montabella Community Schools

Fiduciary Funds

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

Year Ended June 30, 2007

	Private Purpose Trust Fund
ADDITIONS	
Investment earnings	
Interest	\$ 1,463
DEDUCTIONS	-
CHANGE IN NET ASSETS	1,463
Net assets - beginning of year	40,330
Net assets - end of year	\$ 41,793

See accompanying notes to financial statements.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Montabella Community Schools have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The District's more significant accounting policies are described below.

1. Reporting Entity

As required by accounting principles generally accepted in the United States of America; GASB Statement No. 14, *The Financial Reporting Entity* (as amended by GASB Statement No. 39); and *Statement on Michigan Governmental Accounting and Auditing No. 5*, these financial statements present the financial activities of Montabella Community Schools (primary government). The District has no activities that would be classified as component units.

2. Basis of Presentation

DISTRICT-WIDE FINANCIAL STATEMENTS

The statement of net assets and the statement of activities (the district-wide statements) present information for the district as a whole. All non-fiduciary activities of the primary government are included (i.e., fiduciary fund activities are not included in the district-wide statements). Interfund activity has been eliminated in the preparation of the district-wide financial statements.

The district-wide and fiduciary fund financial statements are presented using the economic resources measurement focus, similar to that used by business enterprises or not-for-profit organizations. Because another measurement focus is used in the governmental fund financial statements, reconciliations are provided that explain the differences in detail.

The statement of activities presents the direct functional expenses of the District and the program revenues that support them. Direct expenses are specifically associated with a service, program, or department and are therefore clearly identifiable to a particular function. Program revenues are associated with specific functions and include charges to recipients of goods or services and grants and contributions that are restricted to meeting the operational or capital requirements of that function. Revenues that are not required to be presented as program revenues are general revenues. This includes all taxes, interest, and unrestricted State aid payments and other general revenues and shows how governmental functions are either self-financing or supported by the general revenues of the District.

FUND FINANCIAL STATEMENTS

The District uses funds to maintain its financial records during the year. A fund is defined as a fiscal and accounting entity with a self balancing set of accounts. The District utilizes governmental and fiduciary funds.

The governmental fund financial statements present the District's individual major funds and aggregated nonmajor funds. Separate columns are shown for the major funds on the balance sheet and statement of revenues, expenditures, and changes in fund balances. Nonmajor funds are combined and shown in a single column.

All governmental funds are presented using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

2. Basis of Presentation - continued

The major funds of the District are:

- a. General Fund - The General Fund is used to account for money or other resources provided to the District to support the educational programs and general operations of the District.
- b. Site and Facilities Sinking Fund - The Site and Facilities Sinking Fund is used to account for the construction and repair of the facilities of the District.

3. Measurement Focus

The government-wide and fiduciary private purpose trust fund financial statements are presented using the economic resources measurement focus, similar to that used by business enterprises or not-for-profit organizations. Because another measurement focus is used in the governmental fund financial statements, reconciliations to the government-wide statements are provided that explain the differences in detail.

All governmental funds are presented using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

There is no measurement focus for fiduciary agency fund since assets equal liabilities.

4. Basis of Accounting

Basis of accounting refers to the timing under which transactions are recognized for financial reporting purposes. Governmental fund financial statements use the modified accrual basis of accounting. The district-wide and fiduciary fund financial statements are prepared using the accrual basis of accounting.

Under the accrual basis of accounting, revenue is recorded in the period in which it is earned and expenses are recorded when incurred, regardless of the timing of related cash flows. Property tax revenue is recognized in the fiscal year for which it is levied. Revenues for grants, entitlements, and donations are recognized when all eligibility requirements imposed by the provider have been met. Deferred revenue is recorded when resources are received by the District before it has legal claim to them, such as when grant monies are received prior to the incurrence of qualified expenditures.

Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., when they become both measurable and available). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Revenues susceptible to accrual include property taxes, state and federal aid, and interest revenue. Other revenues are not susceptible to accrual because generally they are not measurable until received in cash. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt which are recorded when due.

The District reports deferred revenue on its governmental funds balance sheet. Deferred revenues arise when potential revenue does not meet both the "measurable" and "available" criteria for recognition in the current period. Resources are considered available if they are collected during the current fiscal year or soon enough afterward to be used in payment of current year liabilities - defined as expected to be received within sixty days of year-end. Deferred revenues also arise when the District receives resources before it has a legal claim to them. In subsequent periods, when both revenue recognition criteria are met, the liability for deferred revenue is removed from the balance sheet and revenue is recognized.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

5. Budgets and Budgetary Accounting

Budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America. Annual appropriated budgets are adopted for the General and Special Revenue funds. All unexpended appropriations lapse at fiscal year-end.

The District follows these procedures in establishing the budgetary data reflected in the financial statements:

- a. The Superintendent submits to the School Board a proposed operating budget for the fiscal year commencing on July 1. The operating budget includes proposed expenditures and the means for financing them.
- b. Public hearings are conducted to obtain taxpayer comments.
- c. Prior to July 1, the budget is legally adopted by School Board resolution pursuant to the Uniform Budgeting and Accounting Act (P.A. 621 of 1978). The Act requires that the budget be amended prior to the end of the fiscal year when necessary to adjust appropriations if it appears that revenues and other financing sources will not be in excess of original estimates. Expenditures shall not be made or incurred, unless authorized in the budget, in excess of the amounts appropriated.
- d. The budgets are legally adopted at the functional level; however, they are maintained at the object level for control purposes. Any revisions that alter the total expenditures at the functional level by more than \$1,500 must be approved by the School Board.
- e. Formal budgetary integration is employed as a management control device during the year for the General and Special Revenue Funds.
- f. The budgets, as presented, have been amended in a legally permissible manner. Supplemental appropriations were made during the year with the last one approved June 18, 2007.

6. Cash, Cash Equivalents, and Investments

Cash and cash equivalents consist of checking, savings, money market accounts, and pooled investment funds. Cash equivalents are recorded at cost, which approximates market value.

Investments consist of certificates of deposit with an original maturity of greater than 90 days. Certificates of deposit are recorded at cost, which approximates market value.

7. Short-term Interfund Receivables/Payables

During the course of operations, numerous transactions occur between individual funds for goods provided or services rendered. These receivables and payables are classified as "due from other funds" and "due to other funds" on the balance sheet.

8. Due From Other Governmental Units

Due from other governmental units consists of various amounts owed to the District for grant programs and State Aid payments. The total amount of \$1,316,157 due from other governmental units consists of \$1,131,404 and \$184,753 related to State Aid and grant and local programs, respectively.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

9. Inventories

Inventories are stated at cost on a first in/first out basis. The Food Services Fund inventory consists of food and paper goods. Inventory amounts are equally offset by a fund balance reserve which indicates that they do not constitute "available spendable resources" even though they are a component of net current assets.

10. Capital Assets

Capital assets include land, buildings, equipment, and vehicles and are recorded (net of accumulated depreciation, if applicable) in the district-wide financial statements. Capital assets are those with an initial individual cost greater than \$5,000 and an estimated useful life of more than one year, except for new computers, printers, data projectors and televisions (which have no cost threshold) and all new classrooms (recorded at total content cost). Capital assets are not recorded in the governmental funds. Instead, capital acquisition and construction are reflected as expenditures in governmental funds. All purchased capital assets are valued at cost where historical records are available and at an estimated historical cost where no historical records exist. Donated capital assets are valued at their estimated fair market value on the date received.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Depreciation is computed using the straight-line method over the following useful lives:

Buildings and improvements	20 - 50 years
Equipment	5 - 20 years
Vehicles	8 years

The District has no assets that would be classified as infrastructure assets.

11. Compensated Absences

Based on the requirements of GASB Statement No. 16, *Accounting for Compensated Absences*, the District has recorded all liabilities associated with compensated absences. Accumulated vested severance amounts and nonvested severance amounts that are probable to vest and be paid at termination are considered payable from future resources and are recorded along with the related payroll taxes as a long-term liability in the district-wide financial statements.

12. Accrued Interest Payable

Accrued interest is presented for long-term obligations in the district-wide statements in two components: the portion of accrued interest payable that is due within one year is reported as a current liability, the remaining amount that is not due within one year has been reported as a noncurrent liability. The interest payable on the Durant Resolution bonds that were due May 15, 2003, 2004, 2005, and 2007, and a portion of the payment that is due May 15, 2008, is shown as a noncurrent liability due to the State of Michigan deferring these payments until May 15, 2010.

13. Short-Term Note Obligations

Short-term debt is recognized as a liability of a governmental fund and is included on the balance sheet of the applicable fund. During the current year the District borrowed funds to meet short-term cash flow borrowing needs. The final payment is due and payable in August 2007, and anticipated State Aid is expected to be sufficient to cover this commitment.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

14. Long-term Obligations

Long-term debt is recognized as a liability in the district-wide statements when incurred. The portion of those liabilities expected to be paid within the next year is a current liability with the remaining amounts shown as long-term.

Long-term debt is recognized as a liability of a governmental fund when due or when resources have been accumulated in the Debt Service Fund for payment early in the following year. For other long-term obligations, only that portion expected to be financed from expendable available financial resources is reported as a fund liability of a governmental fund.

15. Property Taxes

Property taxes levied by the District are collected by various municipalities and periodically remitted to the District. The taxes are levied as of December 1 and are due upon receipt of the billing by the taxpayer. The actual due date is February 14, after which time the bills become delinquent and penalties and interest may be assessed by the collecting entity. School District property tax revenues are recognized when levied to the extent that they result in current revenue (collected as of year-end). Amounts received subsequent to June 30 are recognized as revenue when collected.

The District levied taxes of \$17.8993 per \$1,000 of taxable valuation on nonhomestead property for general governmental services, and \$1.8900 for 1999 Refunding Debt, \$3.5600 for 1999 Building and Site Bonds, and \$1.4916 for a building and site sinking fund per \$1,000 of taxable valuation on the total applicable taxable valuation of all property within the District.

16. State Foundation Revenue

Beginning with the fiscal year ended June 30, 1995, the State of Michigan adopted a foundation grant approach, which provides for a specific annual amount of revenue per student based on a statewide formula. Prior to the fiscal year ended June 30, 1995, the State utilized a district power equalizing approach. The foundation is funded from State and local sources. Revenues from State sources are primarily governed by the School Aid Act and the School Code of Michigan. The Michigan Department of Education administers the allocation of State funds to school districts based on information supplied by the districts. For the year ended June 30, 2007, the foundation allowance was based on the average of pupil membership counts taken in September 2006 and February 2006. The average calculation was weighted 75% for the September 2006 count and 25% for the February 2006 count.

The State portion of the foundation is provided primarily by a State education property tax millage of 6 mills and an allocated portion of State sales and other taxes. The local portion of the foundation is funded primarily by nonhomestead property taxes, which may be levied at a rate of up to 18 mills. The State revenue is recognized during the foundation period (currently the fiscal year) and is funded through nine (9) payments made during the year and two (2) payments made subsequent to year-end. The local revenue is recognized as outlined above under Property Taxes.

17. State Categorical Revenue

The District also receives revenue from the State to administer certain categorical education programs. State rules require that revenue earmarked for these programs be expended for its specific purpose. Categorical funds received which are not expended by the close of the fiscal year are reported as deferred revenue.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

18. Interfund Transactions

Interfund transactions are reported as either loans, services provided, reimbursements or transfers. Loans are reported as interfund receivables and payables as appropriate and are subject to elimination upon consolidation. Services provided, deemed to be at market or near market rates, are treated as revenues and expenditures/expenses. Reimbursements are recorded when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers on the governmental fund financial statements. Transfers are netted as part of the reconciliation to the district-wide financial statements.

19. Comparative Data

Comparative data for the prior year has not been presented in the financial statements since their inclusion would make the statements unduly complex and difficult to read.

20. Federal Programs

Federal programs are accounted for in the General Fund and specific Special Revenue Funds. The District has not integrated its Single Audit reports and financial data as part of the financial statements. The Single Audit reports and financial data will be issued under separate cover as supplementary information to the financial statements.

NOTE B: CASH, CASH EQUIVALENTS, AND INVESTMENTS

In accordance with Michigan Public Act 451 of 1976, Section 1223(1), as amended, the District is authorized to invest its surplus funds in the following types of investments:

1. Bonds, bills, or notes of the United States; obligations, the principal and interest of which are fully guaranteed by the United States; or obligations of the State.
2. Certificates of deposit issued by a state or national bank, savings accounts of a state or federal savings and loan association, or certificates of deposit or share certificates of a state or federal credit union organized and authorized to operate in this state.
3. Commercial paper rated prime at the time of purchase and maturing not more than 270 days after the date of purchase.
4. Securities issued or guaranteed by agencies or instrumentalities of the United States government.
5. United States government or federal agency obligation repurchase agreements.
6. Bankers' acceptances issued by a bank that is a member of the Federal Depository Insurance Corporation.
7. Mutual funds composed entirely of investment vehicles that are legal for direct investment by a School District.
8. Investment pools, as authorized by the Surplus Funds Investment Pool Act, Act No. 367 of the Public Acts of 1982, being sections 129.111 to 129.118 of the Michigan Compiled Laws, composed entirely of instruments that are legal for direct investment by a School District.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE B: CASH, CASH EQUIVALENTS, AND INVESTMENTS - CONTINUED

Michigan Public Acts authorize school districts in Michigan to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations. Deposits of the District are at federally insured banks and credit unions in the State of Michigan in the name of the School District.

Federal Deposit insurance Corporation (FDIC), Federal Savings and Loan Insurance Corporation (FSLIC) and the National Credit Union Administration regulations provide that deposits of governmental units are to be separately insured for savings deposits and demand deposits up to \$100,000 each. Furthermore, if specific deposits are regulated by statute or bond indenture, these specific deposits are to be separately insured for the amount of \$100,000. Michigan School Code Section 1223 allows that security in the form of collateral, surety bond, or another form may be taken for the deposits or investments of a school district in a bank, savings and loan association, or credit union.

Deposits

There is a custodial credit risk as it relates to deposits. In the case of deposits, this is the risk that in the event of a bank failure, the District's deposits may not be returned to it. As of June 30, 2007, the carrying amount of the District's deposits was \$1,363,937 and the bank balance was \$1,794,716 of which \$270,080 was covered by federal depository insurance. The balance of \$1,524,636 was uninsured and uncollateralized. The District had \$100 of imprest cash on hand.

Investments

As of June 30, 2007, the District had the following investments:

<u>Investment type</u>	<u>Fair value</u>	<u>Bank Balance</u>	<u>Weighted Average Maturity</u>
Insured or registered for which the securities are held by the District's name			
Mutual Funds			
Government Fund	\$ 15,106	\$ 15,106	N/A
MILAF+ Cash Management Class	62,129	62,129	N/A
MILAF+ MAX Class	<u>1,239,406</u>	<u>1,239,406</u>	N/A
	<u>\$ 1,316,641</u>	<u>\$ 1,316,641</u>	

Credit risk

State law limits investments in certain types of investments to a prime or better rating issued by nationally recognized statistical rating organizations (NRSRO's). As of June 30, 2007, the District's investments in the Government Fund and the uncategorized pooled investment (the Michigan Liquid Asset Fund Plus) were rated AAAM and AAA by Standard and Poor's, respectively.

Interest rate risk

The District will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities in the open market and investing operating funds primarily in shorter-term securities, liquid asset funds, money market mutual funds, or similar investment pools and limiting the average maturity in accordance with the District's cash requirements.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE B: CASH, CASH EQUIVALENTS, AND INVESTMENTS - CONTINUED

Concentration of credit risk

The District will minimize concentration of credit risk, which is the risk of loss attributed to the magnitude of the District's investment in a single issuer, by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized.

Custodial credit risk

The District will minimize custodial credit risk, which is the risk of loss due to the failure of the security issuer or backer, by limiting investments to the types of securities authorized by the Board and pre-qualifying the financial institutions, broker/dealers, intermediaries and advisors with which the District will do business in accordance with Board approved policy.

As of June 30, 2007, the cash and cash equivalents and investments referred to above have been reported in either the cash and cash equivalents or investments captions in the basic financial statements in the following categories:

	<u>Governmental Activities</u>	<u>Fiduciary Funds</u>	<u>Total Primary Government</u>
Cash and cash equivalents	\$ 2,506,005	\$ 114,946	\$ 2,620,951
Investments	<u>-</u>	<u>59,727</u>	<u>59,727</u>
	<u>\$ 2,506,005</u>	<u>\$ 174,673</u>	<u>\$ 2,680,678</u>

Due to significantly higher cash flow at certain periods during the year, the amount the District held as cash, cash equivalents and investments increased significantly. As a result, the amount of uninsured and uncollateralized cash, cash equivalents, and investments were substantially higher at these peak periods than at year-end.

NOTE C: CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2007 was as follows:

	<u>Balance July 1, 2006</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance June 30, 2007</u>
Vehicles	\$ 67,788	\$ 36,290	\$(28,388)	\$ 75,690
Buildings and improvements	16,716,589	110,578	-	16,827,167
Equipment	<u>2,295,117</u>	<u>45,045</u>	<u>-</u>	<u>2,340,162</u>
Subtotal	19,079,494	191,913	(28,388)	19,243,019
Less accumulated depreciation for:				
Vehicles	(46,497)	-	7,097	(39,400)
Buildings and improvements	(4,944,595)	(366,363)	-	(5,310,958)
Equipment	<u>(1,370,797)</u>	<u>(184,533)</u>	<u>-</u>	<u>(1,555,330)</u>
Subtotal	<u>(6,361,889)</u>	<u>(550,896)</u>	<u>7,097</u>	<u>(6,905,688)</u>
Capital assets, net	<u>\$ 12,717,605</u>	<u>\$(358,983)</u>	<u>\$(21,291)</u>	<u>\$ 12,337,331</u>

Depreciation expense was not allocated to governmental functions. It appears on the statement of activities as "unallocated".

Montabella Community Schools

NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE D: LONG-TERM DEBT

The following is a summary of changes in long-term debt obligations of the District for the year ended June 30, 2007.

	Balance July 1, 2006	Additions	Deletions	Balance June 30, 2007	Amounts Due Within One Year
General Long-Term Debt					
1999 Refunding Bonds	\$ 340,000	\$ -	\$ (340,000)	\$ -0-	\$ -
1998 Durant Resolution Bonds	69,435	-	-	69,435	-
1999 School Building and Site	2,025,000	-	(210,000)	1,815,000	575,000
2005 Refunding Bonds	7,895,000	-	(25,000)	7,870,000	25,000
Other Notes and Loans	1,605	-	(1,605)	-0-	-
Severance Pay	49,558	35,817	(4,110)	81,265	20,316
	10,380,598	35,817	(580,715)	9,835,700	620,316
Less deferred amounts on refunding	(316,459)	-	22,604	(293,855)	(22,604)
	<u>\$10,064,139</u>	<u>\$ 35,817</u>	<u>\$ (558,111)</u>	<u>\$ 9,541,845</u>	<u>\$ 597,712</u>

Significant details regarding outstanding long-term debt (including current portions) are presented below:

General Obligation Bonds

\$10,550,000 1999 Building and Site Bonds dated August 1, 1999, due in annual installments ranging from \$575,000 to \$635,000, with interest of 4.85 percent, payable semi-annually. \$ 1,815,000

\$7,895,000 2005 Refunding Bonds dated July 14, 2005, due in annual installments ranging from \$25,000 to \$805,000, with interest ranging from 3.0 to 4.75 percent, payable semi-annually. 7,870,000

\$ 9,685,000

Resolution Bonds

\$117,596 1998 Durant Resolution Bonds dated November 15, 1998, due in annual installments ranging from \$6,545 to \$40,303 including interest of 4.7615353 percent, payable annually. The annual debt service payments related to these bonds is paid through an annual appropriation from the State of Michigan. The State of Michigan has suspended payment until May 15, 2009. \$ 69,435

Advance Refunding - Prior

On July 14, 2005 the District defeased the portion of the 1999 School Building and Site Bonds, which are due and payable May 1, 2011 through May 1, 2020. This was accomplished by establishing an irrevocable trust with an escrow agent composed of cash and U.S. government securities sufficient to meet the applicable principal and interest obligations. The District issued General Obligation 2005 Refunding Bonds in the amount of \$7,895,000 to provide resources to fund the escrow amounts and pay the costs of issuance of the refunding bonds. Accordingly, the trust account assets and liabilities for the defeased bonds are not included in the District's financial statements. At June 30, 2007, bonds due and payable May 1, 2011 through May 1, 2020 for the 1999 School Building and Site Bonds in the amount of \$7,800,000 are considered defeased.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE D: LONG-TERM DEBT - CONTINUED

Severance Pay

In recognition of services to the District, a severance payment will be made upon termination to eligible employees according to their respective employment contracts or past District practice as follows:

Teachers and Administrative Staff

Employees with at least twelve (12) years of service will be paid up to seventy-five (75) days of accumulated sick days at a rate of \$15 per day.

Support Staff

Employees with at least ten (10) years of service will be paid up to fifty (50) days of accumulated sick days at a rate of \$15 per day.

Under GASB Statement No. 16 requirements, the District has elected to implement the "vesting" method of calculating the compensated absences liability. The amounts accumulated for all employees currently vested are calculated along with an amount for other employees who currently are not vested but are probable to vest in future years. The amounts for employees who currently are not vested are calculated taking total unused sick amounts at June 30, 2007, for all non-vested employees and multiplying it by a historical termination percentage. This percentage is based on an estimate of the percentage of employees who have terminated employment fully vested in the past five (5) years.

A summary of the calculated amounts of accrued severance pay and related payroll taxes as of June 30, 2007, which has been recorded in the District-wide financial statements, is as follows:

	<u>Vested Employees</u>	<u>Non-vested Employees</u>	<u>Total</u>
Severance pay	\$ 55,436	\$ 20,054	\$ 75,490
Payroll taxes	<u>4,241</u>	<u>1,534</u>	<u>5,775</u>
	<u>\$ 59,677</u>	<u>\$ 21,588</u>	<u>\$ 81,265</u>

The annual requirements to pay the debt principal and interest outstanding for the Long-Term Debt are as follows:

<u>Year Ending June 30,</u>	<u>Durant Resolution Bonds</u>		<u>2005 Refunding Bonds</u>		<u>1999 Building and Site Bonds</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2008	\$ -	\$ -	\$ 25,000	\$ 338,748	\$ 575,000	\$ 88,028
2009	6,545	1,714	25,000	337,997	605,000	60,140
2010	40,303	15,181	25,000	337,248	635,000	30,798
2011	7,182	1,076	695,000	336,472	-	-
2012	7,524	734	720,000	308,673	-	-
2013-2017	7,881	375	3,965,000	1,008,963	-	-
2018-2020	<u>-</u>	<u>-</u>	<u>2,415,000</u>	<u>189,577</u>	<u>-</u>	<u>-</u>
	<u>\$ 69,435</u>	<u>\$ 19,080</u>	<u>\$ 7,870,000</u>	<u>\$ 2,857,678</u>	<u>\$ 1,815,000</u>	<u>\$ 178,966</u>

The Durant Resolution Bonds referred to above are bonds whose future debt service payments by the District are contingent on an annual State of Michigan appropriation. This is the only revenue source for making the annual debt service payments on these bonds. If the legislature of the State of Michigan fails to appropriate the funds, in any particular year, the District is under no obligation for payment of that year's debt obligation. The State of Michigan has suspended payments on these bonds until May 15, 2009. It appears this suspension will have no financial impact on Montabella Community Schools in the future.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE E: SHORT-TERM NOTES

On August 18, 2006, the District issued a short-term State School Aid Anticipation Note in the amount of \$1,100,000 for the purpose of funding operating expenditures until the 2007 State Aid payments resumed. This short-term note, which has a net outstanding balance of \$1,100,000 at June 30, 2007, is reported in the General Fund under the caption short-term notes payable. The outstanding balance is due August 20, 2007.

NOTE F: INTERFUND RECEIVABLES AND PAYABLES

The amount of interfund receivables and payables at June 30, 2007, are as follows:

Due to General Fund from:	
Nonmajor governmental funds	\$ <u>105,979</u>

Amounts appearing as interfund payables and receivables arise from two types of transactions. One type of transaction is where a fund will pay for a good or service that at least a portion of the benefit belongs to another fund. The second type of transaction is where one fund provides a good or service to another fund. Balances at the end of the year are for transfers that have not cleared as of the balance sheet date.

NOTE G: INTERFUND TRANSFERS

Permanent reallocation of resources between funds of the reporting entity is classified as interfund transfers. For the purpose of the statement of activities, all interfund transfers between individual governmental funds have been eliminated.

Transfers to nonmajor governmental funds from:	
General Fund	\$ <u>135,999</u>

Transfers to Site and Facilities Sinking Fund from:	
Nonmajor governmental funds	\$ <u>2,374</u>

NOTE H: EMPLOYEE RETIREMENT SYSTEM

All of the District's employees, except students, are eligible to participate in the statewide Michigan Public School Employees' Retirement System (MPERS), a multiple-employer, cost-sharing, statewide public employee retirement system. The MPERS issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. The report for the fiscal year-end September 30, 2006, the last year available, may be obtained by contacting the State of Michigan Department of Management and Budget.

The payroll for employees covered by the MPERS for the year ended June 30, 2007, was \$4,522,909 of which \$3,088,655 was for members who have elected the MIP option; the District's total payroll was \$4,578,397.

Effective January 1, 1987, Act 91 of the Public Acts of 1985 established a voluntary contribution to the Member Investment Plan (MIP). Employees first hired before January 1, 1990, made a one-time irrevocable election to contribute to the tax deferred MIP. For a limited period ended January 1, 1993, an active Basic Plan member may have enrolled in MIP by repaying the contributions and interest that would have been made had MIP enrollment occurred initially prior to January 1, 1990. Employees first hired on or after January 1, 1990, will automatically be included in MIP.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE H: EMPLOYEE RETIREMENT SYSTEM - CONTINUED

Members in MIP may retire at any age after attaining thirty years of credited service, or at age sixty while still working with a minimum total of five years of credited service, with credited service in each of the five school fiscal years immediately preceding the retirement allowance effective date. The retirement allowance is calculated using a formula of 1.5% of the member's final average compensation multiplied by the total number of years of credited service.

Employees who did not elect the MIP option fall under the MPSERS Basic Plan and may retire after attaining age sixty with ten or more years of credited service; or attaining age fifty-five with thirty or more years of credited service; or attaining age fifty-five while still working with at least fifteen but fewer than thirty years of credited service in each of the five school fiscal years immediately preceding the retirement allowance effective date. The retirement allowance is computed using a formula of 1.5% of the average of the highest total earnings during a period of sixty consecutive months (five years) multiplied by the total years to the nearest tenth of a year of credited service.

The MPSERS also provides death and disability benefits and health and medical, dental, vision and hearing insurance coverage. Benefits are established by state statute.

Employees who selected MIP on or before December 31, 1989, contributed 4% from January 1, 1987, to December 31, 1989, and 3.9% thereafter. Employees first hired on or after January 1, 1990, are required to contribute based on a graduated rate: 3% of the first \$5,000; 3.6% of \$5,001 through \$15,000; 4.3% of all wages over \$15,000.

For the period of July 1, 2006 to September 30, 2006, the District was required by State statute to contribute 16.34% of covered compensation for all wages to the Plan. For the period of October 1, 2006 to June 30, 2007 the District was required by State statute to contribute 17.74% of covered compensation for all wages to the Plan.

The total amount contributed to the Plan for the year ended June 30, 2007, and the previous two (2) years is as follows:

<u>June 30,</u>	<u>MIP</u> <u>Contributions</u>	<u>District</u> <u>Contributions</u>	<u>Total</u> <u>Contributions</u>
2007	\$ 119,437	\$ 791,054	\$ 910,491
2006	117,022	752,503	869,525
2005	105,614	644,872	750,486

The following represents contributions as a percentage of the applicable covered payroll for the current and preceding two (2) years:

<u>June 30,</u>	<u>MIP</u> <u>Contributions</u>	<u>District</u> <u>Contributions</u>
2007	3.8 %	17.5 %
2006	3.8	16.0
2005	3.8	14.4

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE I: RISK MANAGEMENT

The District participates in a pool, the MASB-SEG Property and Casualty Pool with other school districts for property, liability, and errors and omissions. The pool is organized under Public Act 138 of 1982, as amended as a governmental group property and casualty self insurance pool. In the event the pool's claims and expenses for a policy year exceed the total normal annual premiums for said years, all members of the specific pool's policy year may be subject to special assessment to make up the deficiency. The District has not been informed of any special assessments being required.

The District also participates in a pool, the SEG Self-Insured Workers' Disability Compensation Fund, with other school districts for workers' compensation losses. The pool is organized under Public Act 317 of 1969, as amended. In the event the pool's claims and expenses for a policy year exceed the total normal annual premiums for said years, all members of the specific pool's policy year may be subject to special assessment to make up the deficiency. The District has not been informed of any special assessments being required.

NOTE J: EXCESS OF EXPENDITURES OVER APPROPRIATIONS

Michigan Public Act 621 of 1978, Section 18 and 19, as amended, provides that a local governmental unit not incur expenditures in excess of the amounts appropriated.

In the body of the budgetary comparison schedule, the District's budgeted expenditures in the General Fund have been adopted and shown at the functional classification level. Budgeted expenditures for nonmajor Special Revenue funds have not been presented.

During the year ended June 30, 2007, the District incurred expenditures in excess of the amounts appropriated as follows:

	<u>Amounts Appropriated</u>	<u>Amounts Expended</u>	<u>Variance</u>
General Fund			
Instruction			
Basic programs			
High school	\$ 1,130,752	\$ 1,133,472	\$ 2,720
Added needs			
Special education	447,021	448,282	1,261
Supporting Services			
Pupil	393,110	425,323	32,213

NOTE K: FUND BALANCE RESERVES

Reserved fund balance is used to earmark a portion of fund balance to indicate that it is not appropriate for expenditures or has been legally segregated for a specific future use.

The following are the various fund balance reserves as of June 30, 2007:

General Fund	
Reserved for prepaids	<u>\$ 6,707</u>
Nonmajor governmental funds	
Reserved for inventories	\$ 9,751
Reserved for debt service	<u>324,393</u>
	<u>\$ 334,144</u>

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2007

NOTE L: RESTRICTED NET ASSETS

Restrictions of net assets shown in the District-wide financial statements indicate that restrictions imposed by the funding source or some other outside source which precludes their use for unrestricted purposes. The following is the net asset restriction as of June 30, 2007:

Governmental activities	
Restricted for debt service	\$ 241,214
Restricted for sinking fund activities	<u>600,526</u>
	<u>\$ 841,740</u>

NOTE M: SPECIAL EDUCATION UNDERFUNDING SETTLEMENT

Prior to the current year the Durant vs. State of Michigan case was settled and the State was required to reimburse each plaintiff and nonplaintiff an agreed upon amount for past underfunding of special education. Montabella Community Schools, a nonplaintiff District, was awarded \$235,193 in the settlement. These funds are being paid as follows:

- a. One-half is being paid over the next ten (10) years, which began November 15, 1998. The restrictions on use of these funds are detailed within State School Aid Act, Section 11F(6). These funds are recorded within the General Fund as categorical State Aid. At the end of the current year all these funds had been expended.
- b. One-half is being paid over the next fifteen (15) years, which began May 15, 1999. The District borrowed this portion of the settlement amount through the Michigan Municipal Bond Authority on November 15, 1998. These funds were recorded as bond proceeds in the Capital Projects Fund. The bond proceeds may be used for any purpose specified in Section 1351 (a) of the Revised School Code. The debt service payments or these bonds are to be made through an annual legislative appropriation. If the State of Michigan legislature fails to make the annual appropriation the District is under no obligation for the debt Payments for that year. The District has pledged the annual State payments to the Michigan Municipal Bond Authority for payment of debt service.

NOTE N: BONDED CONSTRUCTION AND SINKING FUNDS

The Capital Projects Funds of the District include the capital project activities funded by the Middle School Construction Bonds and from local millage for a bond sinking fund. For the expenditures recorded within the Middle School Capital Project Fund, the District has complied with the applicable provisions of Section 1351 (a) of the Revised School Code. For the expenditures recorded within the Site and Facilities Sinking Fund, the District has complied with the applicable provisions of Section 1212 (1) of the Revised School Code and the Michigan Department of Treasury Letter No. 01-95.

NOTE O: FLEXIBLE BENEFITS PLAN

In October 1996 the District approved by Board action to implement a flexible benefits cafeteria plan established under Section 125 of the Internal Revenue Code. The Plan, available to all employees, permits them to receive cash in lieu of medical benefits. The Plan, effective October 1, 1997, provides employees with the opportunity to choose among benefits consisting of cash or health benefits.

The Plan is administered by Montabella Community Schools.

REQUIRED SUPPLEMENTARY INFORMATION

Montabella Community Schools

General Fund

BUDGETARY COMPARISON SCHEDULE

Year Ended June 30, 2007

	Original Budget	Final Amended Budget	Actual	Variance with Final Budget Positive (Negative)
REVENUES				
Local sources	\$ 1,165,128	\$ 1,266,987	\$ 1,305,804	\$ 38,817
State sources	6,497,042	6,532,688	6,660,592	127,904
Federal sources	638,575	587,085	526,808	(60,277)
TOTAL REVENUES	8,300,745	8,386,760	8,493,204	106,444
EXPENDITURES				
INSTRUCTION				
Basic programs				
Preschool	133,132	144,310	139,274	5,036
Elementary	1,295,765	1,332,727	1,314,220	18,507
Middle school	1,165,961	1,184,870	1,177,612	7,258
High school	1,160,005	1,130,752	1,133,472	(2,720)
Alternative education	84,831	95,821	85,322	10,499
Total basic programs	3,839,694	3,888,480	3,849,900	38,580
Added needs				
At-risk	129,416	125,649	94,753	30,896
Special education	432,898	447,021	448,282	(1,261)
Compensatory education	438,782	422,411	418,286	4,125
Vocational education	24,269	24,835	24,771	64
Total added needs	1,025,365	1,019,916	986,092	33,824
TOTAL INSTRUCTION	4,865,059	4,908,396	4,835,992	72,404
SUPPORTING SERVICES				
Pupil	399,803	393,110	425,323	(32,213)
Instructional staff	432,786	349,494	303,990	45,504
General administration	224,719	212,312	208,356	3,956
School administration	456,072	474,060	463,573	10,487
Business services	283,035	293,970	289,309	4,661
Central services	137,596	190,408	143,994	46,414
Pupil transportation	691,916	685,064	679,491	5,573
Operation and maintenance	828,606	745,772	717,645	28,127
Other	2,891	52,026	37,187	14,839
TOTAL SUPPORTING SERVICES	3,457,424	3,396,216	3,268,868	127,348

Montabella Community Schools

General Fund

BUDGETARY COMPARISON SCHEDULE - CONTINUED

Year Ended June 30, 2007

	Original Budget	Final Amended Budget	Actual	Variance with Final Budget Positive (Negative)
DEBT SERVICE				
Principal	\$ 5,000	\$ 1,874	\$ 1,874	\$ -0-
TOTAL EXPENDITURES	<u>8,327,483</u>	<u>8,306,486</u>	<u>8,106,734</u>	<u>199,752</u>
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	(26,738)	80,274	386,470	306,196
OTHER FINANCING SOURCES (USES)				
Other transactions	120,750	166,240	53,309	(112,931)
Transfers to other funds	(125,400)	(138,500)	(135,999)	2,501
Payments to other districts	<u>(153,400)</u>	<u>(185,070)</u>	<u>(143,801)</u>	<u>41,269</u>
TOTAL OTHER FINANCING SOURCES (USES)	<u>(158,050)</u>	<u>(157,330)</u>	<u>(226,491)</u>	<u>(69,161)</u>
NET CHANGE IN FUND BALANCE	(184,788)	(77,056)	159,979	237,035
Fund balance, beginning of year	<u>649,213</u>	<u>649,213</u>	<u>649,213</u>	<u>-0-</u>
Fund balance, end of year	<u>\$ 464,425</u>	<u>\$ 572,157</u>	<u>\$ 809,192</u>	<u>\$ 237,035</u>

OTHER SUPPLEMENTARY INFORMATION

Montabella Community Schools

Nonmajor Governmental Funds

COMBINING BALANCE SHEET

June 30, 2007

	Special Revenue Funds		Debt
	Food	Athletics	1999
	Service		Refunding
			Bonds
ASSETS			
Cash and cash equivalents	\$ 178,342	\$ 5,104	\$ 73,517
Accounts receivable	-	195	-
Inventories	9,751	-	-
TOTAL ASSETS	<u>\$ 188,093</u>	<u>\$ 5,299</u>	<u>\$ 73,517</u>
LIABILITIES AND FUND BALANCES			
LIABILITIES			
Accounts payable	\$ 27,622	\$ -	\$ -
Due to other funds	104,395	-	1,584
Due to other governmental units	-	-	2,892
TOTAL LIABILITIES	132,017	-0-	4,476
FUND BALANCES			
Reserved for			
Inventories	9,751	-	-
Debt service	-	-	69,041
Unreserved			
Undesignated, reported in:			
Special revenue funds	46,325	5,299	-
Capital projects funds	-	-	-
TOTAL FUND BALANCES	<u>56,076</u>	<u>5,299</u>	<u>69,041</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 188,093</u>	<u>\$ 5,299</u>	<u>\$ 73,517</u>

Service Funds	Capital Projects Fund	Total Nonmajor Governmental Funds
Middle School Debt	Middle School	
\$ 255,352	\$ 72	\$ 512,387
-	-	195
-	-	9,751
<u>\$ 255,352</u>	<u>\$ 72</u>	<u>\$ 522,333</u>
\$ -	\$ -	\$ 27,622
-	-	105,979
-	-	2,892
<u>-0-</u>	<u>-0-</u>	<u>136,493</u>
-	-	9,751
255,352	-	324,393
-	-	51,624
-	72	72
<u>255,352</u>	<u>72</u>	<u>385,840</u>
<u>\$ 255,352</u>	<u>\$ 72</u>	<u>\$ 522,333</u>

Montabella Community Schools

Nonmajor Governmental Funds

COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCES

Year Ended June 30, 2007

	Special Revenue Funds		Debt
	Food Service	Athletics	1999 Refunding Bonds
REVENUES			
Local sources	\$ 145,598	\$ 43,470	\$ 367,650
State sources	37,207	-	-
Federal sources	264,651	-	-
TOTAL REVENUES	447,456	43,470	367,650
EXPENDITURES			
Current			
Food service	413,832	-	-
Athletics	-	189,346	-
Debt service			
Principal retirement	-	-	340,000
Interest, fiscal and other charges	-	-	15,149
TOTAL EXPENDITURES	413,832	189,346	355,149
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	33,624	(145,876)	12,501
OTHER FINANCING SOURCES (USES)			
Transfers from other funds	-	135,999	-
Transfers to other funds	-	-	-
TOTAL OTHER FINANCING SOURCES (USES)	-0-	135,999	-0-
NET CHANGE IN FUND BALANCES	33,624	(9,877)	12,501
Fund balances, beginning of year	22,452	15,176	56,540
Fund balances, end of year	<u>\$ 56,076</u>	<u>\$ 5,299</u>	<u>\$ 69,041</u>

<u>Service Funds</u>	<u>Capital Projects Fund</u>	<u>Total Nonmajor Governmental Funds</u>
<u>Middle School Debt</u>	<u>Middle School</u>	
\$ 669,977	\$ 11	\$ 1,226,706
-	-	37,207
-	-	264,651
669,977	11	1,528,564
-	-	413,832
-	-	189,346
235,000	-	575,000
440,529	-	455,678
675,529	-0-	1,633,856
(5,552)	11	(105,292)
-	-	135,999
-	(2,374)	(2,374)
-0-	(2,374)	133,625
(5,552)	(2,363)	28,333
260,904	2,435	357,507
<u>\$ 255,352</u>	<u>\$ 72</u>	<u>\$ 385,840</u>

Principals

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Education
Montabella Community Schools
Edmore, Michigan

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of and for the year ended June 30, 2007, which collectively comprise Montabella Community Schools' basic financial statements and have issued our report thereon dated September 13, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Montabella Community Schools' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of Montabella Community Schools' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Montabella Community Schools' internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the District's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the District's financial statements that is more than inconsequential will not be prevented or detected by the District's internal control. We consider the deficiencies described below to be significant deficiencies in internal control over financial reporting.

2007-1 PREPARATION OF FINANCIAL STATEMENTS IN ACCORDANCE WITH GAAP

Criteria: Governments are required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). Responsibility for the financial statements of the District rests with the District's management. The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing, and summarizing accounting data (i.e., maintaining internal accounting records), and (2) reporting government-wide and fund financial statements, including the related note disclosures (i.e., external financial reporting).

Condition: It has historically been common for many governments to rely on the independent auditors to assist in the preparation of the government-wide and fund financial statements, as well as the related notes to the financial statements, as part of its external financial reporting process. As a result, a government's ability to prepare financial statements in accordance with GAAP has typically been based, in part, on its reliance on the independent auditors. By definition, independent auditors cannot be part of the government's internal controls.

2007-1 PREPARATION OF FINANCIAL STATEMENTS IN ACCORDANCE WITH GAAP - CONTINUED

The condition noted in the preceding paragraph exists at Montabella Community Schools. The cause for this condition is simply because it is more cost effective to outsource the preparation of its annual financial statements to the independent auditors than to incur the time and expense of having the employees and/or management obtain the necessary training and expertise required to perform this task internally.

Effect: As a result of this condition, the employees and/or management do not possess the qualifications necessary to prepare the District's annual financial statements and notes to the financial statements in accordance with GAAP. The District relies, in part, on the independent auditors for assistance with the preparation of annual financial statements and related notes to the financial statements in accordance with GAAP.

Recommendation: We recommend the District consider obtaining proper training for the appropriate members of the District's administration to assure that they are able to fully understand the requirements of preparing GAAP financial statements. This understanding is essential for the District's administration to be able to accept responsibility for the amounts and disclosures included in the District's financial statements.

Corrective Action Response: Management of the District is aware of this deficiency and will continue to look for opportunities to increase our understanding of the requirements of preparing GAAP financial statements. However, at this time we believe it is not cost beneficial in our situation to develop this expertise. We will continue to use our external auditors for this technical assistance. We would expect this situation to be ongoing in future years.

2007-2 MATERIAL JOURNAL ENTRIES PROPOSED BY AUDITORS

Criteria: Statement on Auditing Standards No. 112 (SAS 112), *Communicating Internal Control Related Matters Identified in an Audit*, emphasizes that management is responsible for establishing, maintaining, and monitoring internal controls, and for the fair presentation in the financial statements of financial position, results of operations, and cash flows (when applicable), including the notes to financial statements, in conformity with U.S. generally accepted accounting principles. The auditor cannot be a part of internal controls.

Condition: Material journal entries for the adjustment of cash, state aid and grant revenue, and accounts receivable were proposed by the auditors. These misstatements were not detected by the District's internal control over financial reporting.

Effect: Through the identification of material journal entries that were not otherwise identified by management, the auditors are effectively part of the District's internal controls.

Recommendation: We recommend that the District take steps to ensure that material journal entries are not necessary at the time future audit analysis is performed.

Corrective Action Response: Management of the District is currently reviewing procedures related to identification and correction of potential errors in the financial statements.

2007-3 UNTIMELY BANK DEPOSITS

Criteria: To strengthen and improve internal control over and safeguarding of assets, deposits to financial institutions must be made in a timely manner.

Condition: During the course of our audit, it was noted that a significant amount received in June was held on hand and not deposited until August.

Effect: The District is not in compliance with the District's receipt and deposit procedures. Furthermore, it could be an indication of a problem in the District's internal control over and safeguarding of assets.

Recommendation: We recommend the District review its receipt and deposit procedures to ensure that all receipts are deposited to the bank in a timely manner.

Corrective Action Response: This untimely deposit was an isolated incident and is it is not the regular practice of the District to hold deposits for an extended period of time. Management of the District will review it's procedures related to prompt deposit of funds received to ensure that this incident is not repeated.

2007-4 UNRECORDED ADDITIONS IN CAPITAL ASSET STATEMENTS PREPARED BY APPRAISAL COMPANY

Criteria: According to the Accounting Procedures Manual for Local Units of Government in Michigan, "the recording of capital assets makes it possible to provide for protective custody and to fix responsibility for proper use and custody of such assets. It also permits proper disclosure on financial statements, for no financial report is complete without reflecting the capital assets of a local unit."

Condition: During the course of our audit, we have noted that material amounts of capital asset additions were not recorded in the asset statements prepared by the Appraisal Company, including some assets that were noted during our audit last year.

Effect: Through the identification of material additions in capital assets that were not otherwise identified by management, the auditors are effectively part of the District's internal controls. In addition, the District is not in compliance with the capital asset policy established by the Board.

Recommendation: Responsibility for the fair presentation of the District's financial statements, including the amounts and disclosures within the financial statements, rests with the District's management. The District should establish sufficient internal controls to assure that the capital assets are recorded in the statements prepared by the Appraisal Company in accordance with the District's capital assets policy.

Corrective Action Response: Management of the District will work with the appraisal company to ensure that significant improvements and items purchased, meeting the District's criteria for capitalization, will be included in the District's annual asset appraisal.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the District's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. We believe that the significant deficiencies described above as 2007-1, 2007-2, 2007-3, and 2007-4 are material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Montabella Community Schools' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which are described below.

2007-5 THE USE OF THE DISTRICT'S NAME AND/OR EMPLOYER IDENTIFICATION NUMBER BY OTHER ENTITIES

Criteria: According to the Michigan Public School Accounting Manual, "Cash and bank accounts in use should be only those authorized by the school board and use should be for authorized purposes."

Condition: During the course of our audit, we noted that several organizations/entities independent of the District (i.e., PTO, Junior Achievement, boosters, etc.) hold deposit accounts with local banks under the name and/or employer identification number of the District. This issue was noted and reported in our audit comments last year.

Effect: The District is associated with certain bank accounts, yet the District does not include these accounts in the District's general ledger and does not reconcile and monitor these accounts. Ultimately, the District cannot establish internal control over such assets.

Recommendation: We recommend the District contact the banks with which it does business and take the necessary steps to have the District's identifying information removed from all accounts not under the control of the District.

2007-5 THE USE OF THE DISTRICT'S NAME AND/OR EMPLOYER IDENTIFICATION NUMBER BY OTHER ENTITIES - CONTINUED

Corrective Action Response: The District has made significant improvement in this area since it was first reported. We will continue to work with these organizations to ensure that identifying information of the District is removed from the accounts of these independent organizations or take steps incorporate these accounts in the District's annual financial audit.

2007-6 UNFAVORABLE BUDGET VARIANCES

Criteria: The Uniform Budgeting and Accounting Act requires the District to amend the original adopted budget "as soon as it becomes apparent that a deviation from the original general appropriations act is necessary and the amount of the deviation can be determined". The Act also states that "an administrative officer of the local unit shall not incur expenditures against an appropriation account in excess of the amount appropriated by the legislative body".

Condition: During our review of the District's compliance with the budgeting act, we noted that expenditures had exceeded the amounts appropriated for various activities in the General Fund.

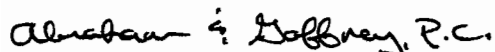
Effect: The District adopted the budget for the General Fund at the functional. Having unfavorable budget variances as described above, the District is not in compliance with Public Act 621 of 1978, as amended.

Recommendation: We recommend the District monitor expenditures against adopted budgets in all applicable funds and make appropriate budget amendments as needed.

Corrective Action Response: Management of the District is currently reviewing procedures related to budgetary compliance in accordance with State law.

Montabella Community Schools' responses to the findings identified in our audit are described above. We did not audit Montabella Community Schools' responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management, the Board of Education of Montabella Community Schools, others within the District, and the Federal award agencies and is not intended to be, and should not be, used by anyone other than these specified parties.



ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

September 13, 2007

Montabella Community Schools

**SUPPLEMENTARY INFORMATION
TO FINANCIAL STATEMENTS
(FEDERAL AWARDS)**

June 30, 2007

Montabella Community Schools

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Education
Montabella Community Schools
Edmore, Michigan

Compliance

We have audited the compliance of Montabella Community Schools with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that is applicable to the major Federal program for the year ended June 30, 2007. Montabella Community Schools' major Federal program is identified in the summary of auditor's results section of the accompanying schedule of findings. Compliance with the requirements of laws, regulations, contracts and grants applicable to the major Federal programs is the responsibility of Montabella Community Schools' management. Our responsibility is to express an opinion on Montabella Community Schools' compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Nonprofit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major Federal program occurred. An audit includes examining, on a test basis, evidence about Montabella Community Schools' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Montabella Community Schools' compliance with those requirements.

In our opinion, Montabella Community Schools complied, in all material respects, with the requirements referred to above that are applicable to the major Federal program for the year ending June 30, 2007.

Internal Control Over Compliance

The management of Montabella Community Schools is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to Federal programs. In planning and performing our audit, we considered Montabella Community Schools' internal control over compliance with requirements that could have a direct and material effect on a major Federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing our opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Montabella Community Schools' internal control over compliance.

A control deficiency in an district's internal control over compliance exists when the design or operation of a control does not allow management or employee's, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the District's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the District's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the District's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of and for the year ended June 30, 2007, and have issued our report thereon dated September 13, 2007. Our audit was performed for the purpose of forming our opinions on the financial statements that collectively comprise Montabella Community Schools' basic financial statements. The accompanying schedule of expenditures of Federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Board of Education and management of Montabella Community Schools, the pass-through grantors, and the Federal awarding agencies and is not intended to be used by anyone other than these specified parties.

Abraham & Gaffney, P.C.

ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

September 13, 2007

Montabella Community Schools

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2007

Federal Grantor / Pass-Through Grantor Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Restated Program or Award Amount	(Memo Only) Prior Years' Expenditures	Balance July 1, 2006 Accrued or (Deferred) Revenue	Cash Receipts In-Kind Payments	Expenditures	Balance June 30, 2007 Accrued or (Deferred) Revenue
U.S DEPARTMENT OF EDUCATION								
Passed Through State Department of Education								
Title I Grants to Local Educational Agencies	84.010 ^(e)							
2005-06 Carryover		0615300607	\$ 65,155	\$ -	\$ -	\$ 32,374	\$ 65,155	\$ 32,781
2005-06 Regular		0615300506	304,161	304,161	53,834	53,834	-	-0-
2006-07 Regular		0715300607	333,769	-	-	221,550	285,085	63,535
			703,085	304,161	53,834	307,758	350,240	96,316
Special Education Grants to States	84.027A							
2006-07		0704400607	4,000	-	-	-	2,110	2,110
Title V I.E.P.S.	84.298							
2006-07 Regular		0702500607	2,121	-	-	1,649	2,121	472
Technology Literacy Challenge Grants	84.318							
2006-07 - Regular		0542900405	3,422	-	-	1,500	1,500	-0-
2005-06 - Carryover		0642900607	587	-	-	-	587	587
2005-06 - Regular		0642900506	6,303	6,303	2,111	2,111	-	-0-
			10,312	6,303	2,111	3,611	2,087	587
Comprehensive School Reform Demonstration	84.332							
2006-07		0618700607	94,000	-	-	70,434	73,148	2,714
2005-06		0518700506	94,000	90,369	10,884	10,884	-	-0-
			188,000	90,369	10,884	81,318	73,148	2,714
Improving Teacher Quality	84.367							
2006-07		0705200607	104,451	-	-	40,251	91,738	51,487

Montabella Community Schools

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - CONTINUED

Year Ended June 30, 2007

Federal Grantor / Pass-Through Grantor Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Restated Program or Award Amount	(Memo Only) Prior Years' Expenditures	Balance July 1, 2006 Accrued or (Deferred) Revenue	Cash Receipts In-Kind Payments	Expenditures	Balance June 30, 2007 Accrued or (Deferred) Revenue
U.S. DEPARTMENT OF EDUCATION - CONTINUED								
Passed Through State Department of Education and Kent Intermediate School District								
Safe and Drug-Free Schools and Communities	84.186A							
2006-07		0728600607	\$ 220	\$ -	\$ -	\$ 220	\$ 220	\$ -0-
2005-06		0628600607	8,242	4,050	-	5,144	5,144	-0-
			8,462	4,050	-0-	5,364	5,364	-0-
TOTAL U.S. DEPARTMENT OF EDUCATION			1,020,431	404,883	66,829	439,951	526,808	153,686
U.S. DEPARTMENT OF AGRICULTURE								
Passed Through State Department of Education								
National School Breakfast Program	10.553 ^(f)							
2006-07		071970	61,258	-0-	-0-	61,258	61,258	-0-
2005-06		061970	65,082	57,176	-	7,906	7,906	-0-
			126,340	57,176	-0-	69,164	69,164	-0-
National School Lunch Program	10.555 ^(f)							
2006-07		071950,071960	159,943	-	-	159,943	159,943	-0-
2005-06		061950,061960	167,889	146,486	-	21,403	21,403	-0-
			327,832	146,486	-0-	181,346	181,346	-0-
Food Donation ^(a)	10.550	59045						
Entitlement commodities								
2006-07			14,068	-	-	14,068	14,068 ^(c)	-0-
Bonus commodities								
2006-07			73	-	-	73	73 ^(c)	-0-
			14,141	-0-	-0-	14,141	14,141	-0-
TOTAL U.S. DEPARTMENT OF AGRICULTURE			468,313	203,662	-0-	264,651	264,651	-0-
TOTAL FEDERAL AWARDS			\$ 1,488,744	\$ 608,545	\$ 66,829	\$ 704,602 ^(d)	\$ 791,459 ^(b)	\$ 153,686

Montabella Community Schools

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2007

NOTE A: BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the Federal grant activity of Montabella Community Schools and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Nonprofit Organizations*.

NOTE B: SUMMARY OF SIGNIFICANT EXPLANATIONS OF SCHEDULE

The following descriptions identified below as (a) through (g) represent explanations that cross reference to amounts on the Schedule of Expenditures of Federal Awards.

- (a) The current year revenues for the Food Donation Program are determined based on the 2002/03 guidance provided in the Michigan Department of Education Administrative Policy Number 7. The amounts reported in this schedule as commodities received were taken from the Recipient Entitlement Balance Report, which are in agreement in all material respects with the District's reported amounts.
- (b) The expenditures reported in this schedule are in agreement with the amounts reported in the financial statements and financial reports. The financial reports tested, including claims for advances and reimbursements, were materially correct, complete, accurate, and timely and contain information that is supported by the books and records from which the financial statements have been prepared.
- (c) The amount of out of conditioned commodities due to spoilage or shrinkage included in expenditures is immaterial to the Schedule of Expenditures of Federal Awards taken as a whole.
- (d) The amounts reported in this schedule as cash received are in agreement with the current payment amounts in the Grants Section Auditor's Report.
- (e) Denotes program tested as "major program".
- (f) Denotes programs required to be clustered by the United States Department of Agriculture.
- (g) Agrees to total revenues from Federal sources per financial statements.

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Education
Montabella Community Schools
Edmore, Michigan

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of and for the year ended June 30, 2007, and have issued our report thereon dated September 13, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Montabella Community School's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the District's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the District's financial statements that is more than inconsequential will not be prevented or detected by the District's internal control. We consider the deficiencies described as findings 2007-1, 2007-2, 2007-3, and 2007-4 in the accompanying Schedule of Findings to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the District's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that findings 2007-1, 2007-2, 2007-3, and 2007-4 of the significant deficiencies described in the Schedule of Findings are material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings as findings 2007-4, 2007-5, and 2007-6.

The District's responses to the findings identified in our audit are described in the schedule of findings. We did not audit the District's responses and, accordingly, we express no opinion on them.

This report is intended for the information and use of the Board of Education and management of Montabella Community Schools, the pass-through grantors, and Federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.



ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

September 13, 2007

Montabella Community Schools

SCHEDULE OF FINDINGS

Year Ended June 30, 2007

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified? X Yes No

Significant deficiency(s) identified that are not considered to be material weakness(es)? Yes X None reported

Noncompliance material to financial statements noted? X Yes No

Federal Awards

Internal control over major programs:

Material weakness(es) identified? Yes X No

Significant deficiency(s) identified that are not considered to be material weakness(es)? Yes X None reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported with Section 501(a) of Circular A-133? Yes X No

Identification of major programs:

CFDA Number(s)	Name of Federal Program or Cluster
84.010	Title I

Dollar threshold used to distinguish between Type A and Type B programs: \$ 300,000

Auditee qualified as low-risk auditee? X Yes No

Section II - Financial Statement Findings

2007-1 PREPARATION OF FINANCIAL STATEMENTS IN ACCORDANCE WITH GAAP

Criteria: Governments are required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). Responsibility for the financial statements of the District rests with the District's management. The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing, and summarizing accounting data (i.e., maintaining internal accounting records), and (2) reporting government-wide and fund financial statements, including the related note disclosures (i.e., external financial reporting).

Condition: It has historically been common for many governments to rely on the independent auditors to assist in the preparation of the government-wide and fund financial statements, as well as the related notes to the financial statements, as part of its external financial reporting process. As a result, a government's ability to prepare financial statements in accordance with GAAP has typically been based, in part, on its reliance on the independent auditors. By definition, independent auditors cannot be part of the government's internal controls.

Section II - Financial Statement Findings - Continued

2007-1 PREPARATION OF FINANCIAL STATEMENTS IN ACCORDANCE WITH GAAP - CONTINUED

The condition noted in the preceding paragraph exists at Montabella Community Schools. The cause for this condition is simply because it is more cost effective to outsource the preparation of its annual financial statements to the independent auditors than to incur the time and expense of having the employees and/or management obtain the necessary training and expertise required to perform this task internally.

Effect: As a result of this condition, the employees and/or management do not possess the qualifications necessary to prepare the District's annual financial statements and notes to the financial statements in accordance with GAAP. The District relies, in part, on the independent auditors for assistance with the preparation of annual financial statements and related notes to the financial statements in accordance with GAAP.

Recommendation: We recommend the District consider obtaining proper training for the appropriate members of the District's administration to assure that they are able to fully understand the requirements of preparing GAAP financial statements. This understanding is essential for the District's administration to be able to accept responsibility for the amounts and disclosures included in the District's financial statements.

Corrective Action Response: Management of the District is aware of this deficiency and will continue to look for opportunities to increase our understanding of the requirements of preparing GAAP financial statements. However, at this time we believe it is not cost beneficial in our situation to develop this expertise. We will continue to use our external auditors for this technical assistance. We would expect this situation to be ongoing in future years.

2007-2 MATERIAL JOURNAL ENTRIES PROPOSED BY AUDITORS

Criteria: Statement on Auditing Standards No. 112 (SAS 112), *Communicating Internal Control Related Matters Identified in an Audit*, emphasizes that management is responsible for establishing, maintaining, and monitoring internal controls, and for the fair presentation in the financial statements of financial position, results of operations, and cash flows (when applicable), including the notes to financial statements, in conformity with U.S. generally accepted accounting principles. The auditor cannot be a part of internal controls.

Condition: Material journal entries for the adjustment of cash, state aid and grant revenue, and accounts receivable were proposed by the auditors. These misstatements were not detected by the District's internal control over financial reporting.

Effect: Through the identification of material journal entries that were not otherwise identified by management, the auditors are effectively part of the District's internal controls.

Recommendation: We recommend that the District take steps to ensure that material journal entries are not necessary at the time future audit analysis is performed.

Corrective Action Response: Management of the District is currently reviewing procedures related to identification and correction of potential errors in the financial statements.

2007-3 UNTIMELY BANK DEPOSITS

Criteria: To strengthen and improve internal control over and safeguarding of assets, deposits to financial institutions must be made in a timely manner.

Condition: During the course of our audit, it was noted that a significant amount received in June was held on hand and not deposited until August.

Effect: The District is not in compliance with the District's receipt and deposit procedures. Furthermore, it could be an indication of a problem in the District's internal control over and safeguarding of assets.

Recommendation: We recommend the District review its receipt and deposit procedures to ensure that all receipts are deposited to the bank in a timely manner.

Corrective Action Response: This untimely deposit was an isolated incident and is not the regular practice of the District to hold deposits for an extended period of time. Management of the District will review its procedures related to prompt deposit of funds received to ensure that this incident is not repeated.

Section II - Financial Statement Findings - Continued

2007-4 UNRECORDED ADDITIONS IN CAPITAL ASSET STATEMENTS PREPARED BY APPRAISAL COMPANY

Criteria: According to the Accounting Procedures Manual for Local Units of Government in Michigan, "the recording of capital assets makes it possible to provide for protective custody and to fix responsibility for proper use and custody of such assets. It also permits proper disclosure on financial statements, for no financial report is complete without reflecting the capital assets of a local unit."

Condition: During the course of our audit, we have noted that material amounts of capital asset additions were not recorded in the asset statements prepared by the Appraisal Company, including some assets that were noted during our audit last year.

Effect: Through the identification of material additions in capital assets that were not otherwise identified by management, the auditors are effectively part of the District's internal controls. In addition, the District is not in compliance with the capital asset policy established by the Board.

Recommendation: Responsibility for the fair presentation of the District's financial statements, including the amounts and disclosures within the financial statements, rests with the District's management. The District should establish sufficient internal controls to assure that the capital assets are recorded in the statements prepared by the Appraisal Company in accordance with the District's capital assets policy.

Corrective Action Response: Management of the District will work with the appraisal company to ensure that significant improvements and items purchased, meeting the District's criteria for capitalization, will be included in the District's annual asset appraisal.

2007-5 THE USE OF THE DISTRICT'S NAME AND/OR EMPLOYER IDENTIFICATION NUMBER BY OTHER ENTITIES

Criteria: According to the Michigan Public School Accounting Manual, "Cash and bank accounts in use should be only those authorized by the school board and use should be for authorized purposes."

Condition: During the course of our audit, we noted that several organizations/entities independent of the District (i.e., PTO, Junior Achievement, boosters, etc.) hold deposit accounts with local banks under the name and/or employer identification number of the District. This issue was noted and reported in our audit comments last year.

Effect: The District is associated with certain bank accounts, yet the District does not include these accounts in the District's general ledger and does not reconcile and monitor these accounts. Ultimately, the District cannot establish internal control over such assets.

Recommendation: We recommend the District contact the banks with which it does business and take the necessary steps to have the District's identifying information removed from all accounts not under the control of the District.

Corrective Action Response: The District has made significant improvement in this area since it was first reported. We will continue to work with these organizations to ensure that identifying information of the District is removed from the accounts of these independent organizations or take steps incorporate these accounts in the District's annual financial audit.

2007-6 UNFAVORABLE BUDGET VARIANCES

Criteria: The Uniform Budgeting and Accounting Act requires the District to amend the original adopted budget "as soon as it becomes apparent that a deviation from the original general appropriations act is necessary and the amount of the deviation can be determined". The Act also states that "an administrative officer of the local unit shall not incur expenditures against an appropriation account in excess of the amount appropriated by the legislative body".

Condition: During our review of the District's compliance with the budgeting act, we noted that expenditures had exceeded the amounts appropriated for various activities in the General Fund.

Section II - Financial Statement Findings - Continued

2007-6 UNFAVORABLE BUDGET VARIANCES - CONTINUED

Effect: The District adopted the budget for the General Fund at the functional. Having unfavorable budget variances as described above, the District is not in compliance with Public Act 621 of 1978, as amended.

Recommendation: We recommend the District monitor expenditures against adopted budgets in all applicable funds and make appropriate budget amendments as needed.

Corrective Action Response: Management of the District is currently reviewing procedures related to budgetary compliance in accordance with State law.

Section III - Federal Award Findings and Questioned Costs

None

Montabella Community Schools

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year Ended June 30, 2007

There were no findings disclosed for the past two years.